of increases to their subscribers."[37] However, the Commission failed to analyze the forces in the marketplace that may promote or inhibit these purported abuses.[38]

The fact that affiliated cable networks sell to thousands of third parties (including other MSOs and cable competitors) eliminates the opportunity for affiliated MSOs to pass through artificially inflated costs to subscribers. The use of sales prices to third parties as a market test has already been adopted by the Commission in the context of other regulated industry affiliate transactions. The Commission thus has allowed telephone companies to book the entire cost of services purchased through affiliated entities as long as the affiliated entity makes sales to third parties.[39] In Separation of Costs of Regulated Telephone Service From Costs of Nonregulated Activities,[40] the Commission ruled that services provided by an unregulated telephone company affiliate to the regulated telephone company are deemed reasonable, and may be recorded in the regulated firm's books at the price paid if that price reflects the same prices charged by the affiliate/supplier to

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[37] Id.

[38] Indeed, in its Program Access rules, the Commission has articulated the fear that affiliated programmers are charging preferentially low rates to their integrated cable operators. The Commission cannot have it both ways.

[39] See 47 C.F.R. 32.27(d).

[40] 2 FCC Rcd. 1298 (1987).

third parties.[41] The Commission's rationale was that unregulated telephone company affiliate sales to third parties "[p]rovided reasonable assurance that the price of assets transferred would not be manipulated to the detriment of ratepayers."[42]

The Commission should afford similar treatment to affiliated cable programming networks because all affiliated programmers hold themselves out and sell their products to third parties. There is no logical basis upon which to distinguish the treatment of telephone company affiliated transactions, and thus disparate treatment cannot hold as a matter of law.[43]

IV. THE COMMISSION HAS NEEDLESSLY IMPEDED CABLE ADVERTISING

The Commission's undue emphasis on use of "the total bill" in operator advertisements will unnecessarily hamper cable operators' ability to market their services efficiently. The Commission has stated that "an operator may not quote a rate for cable service in advertisements and other promotional materials that does not include costs itemized pursuant to section 622(c)."[44] In other words, cable operators will only be allowed to quote a rate for a cable service that reflects the total bill,

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[41] Id. at ¶ 1336.

[42] Reconsideration of Separation of Costs of Regulated Telephone Service From Costs of Nonregulated Activities, 2 FCC Rcd. 6283, 6293 (1987).

[43] See New Orleans Channel 20, Inc., et al., v. FCC, 830 F.2d 361 (1987).

[44] Rate Order at n. 1415.

including all itemized costs.[45] The Commission erects the avoidance of "needless confusion on the part of consumers" as the rationale for this decision.[46] Curiously, however, the hypothetically "confused" subscribers the Commission postulates are a far cry from the actual subscribers with whom TCI interacts daily and who every day encounter numerous advertisements of myriad vendors, many of which market their products or services as, for example, "$15, plus tax," "$19.95, plus shipping and handling," "$8.99, plus freight."

Indeed, even the regulated local telcos utilize such "cost, plus" approaches in their promotional materials. For example, as the duplicate of a C&P subscriber mailing contained in the appendix illustrates, the "Answer Call Telephone Message Service" is offered to the subscriber "for as little as $6.50 a month." A separate part of the mailing informs the subscriber that "all rates and charges are for residential service, are before taxes, if applicable, and are subject to change."

Similarly, cable operators should be permitted to advertise a service as, for example, "$15 plus local governmental fees and taxes." Nothing in the Act authorizes and nothing about the operators provide service over multiple local jurisdictions[47] -- each with distinct franchise fees, PEG access costs, taxes, and other requirements -- the marketing of cable services under the Commission's new rules would be nearly impossible. At great expense and difficulty, cable operators would have to tailor each advertisement and piece of promotional material for each cable service to each community of a system rather than being able to capture the scale economies inherent in regional advertising.

V. "TIER NEUTRAL" RATE REGULATION SCHEME

The Commission rejected arguments of many commenters that the Act requires rates for cable programming services to be regulated under a "bad actor" standard in favor of a "tier are fully before the Commission, and will only briefly be addressed here. Rather, TCI addresses the serious implications of the Commission's abrogation of the statutory plan.

A. A Tier Neutral Scheme Will Have Unintended, Adverse Effects on Cable Programming Services

The Commission's tier neutral rate regulation scheme cannot for over-the-air distribution.[51] But the availability and quality of cable programming services may be radically altered. The economically rational adaptive response to overly aggressive rate regulation of such services is curtailment of delivery of new services and a re-examination of the profitability of presently offered cable programming services.[52] Put simply, benchmark regulation of all cable programming services, and especially the benchmarks derived through the Commission's extraordinarily shaky econometric undertaking,[53] will create incentives to reduce costs by reducing quality.

A tier-specific rate scheme substantially reduces this potential. A cable operator would have the ability to offer on a cable programming tier those programming services which overregulation would make unprofitable to place on the basic tier. This preserves both programming diversity and consumer choice while still providing consumers with basic access to cable. Further, protection against egregious pricing of cable programming services is given by the opportunity for complaint.

The social costs of overregulating are all the more pronounced because of the flawed methodology the Commission used

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[51] Indeed, 40% of all television households still receive their broadcast television programming exclusively through over the air signals.

[52] Low margin, "niche" programming is most likely to be

to derive its benchmarks. Under a scheme that permitted pervasive regulation of the basic tier only, imprecision in the science of calculating the benchmarks could be tolerated even though the level of imprecision in the Commission's quantitative effort is exceedingly high.[54] But the negative effects of this imprecision are far more damaging and invasive if the benchmarks are extended to cable programming services.

The Act's dual regulatory scheme was not merely intended by Congress to allocate workloads evenly between the local authorities and the FCC. The decision to keep cable programming services safe from local regulation was a substantive decision to further the availability of cable programming services. If a franchising authority were allowed to set such rates it might be sorely tempted to peg them artificially low. It would do so on the belief that the cable operator would "make up the difference" by exacting higher fees from a less vigilant franchising authority.[55] As Drs. Besen, Brenner and Woodbury noted, "By giving the Commission the authority over rates for cable program services, Congress may have been signaling its concern that excessively low rates could adversely affect the supply of

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[54] Id.

[55] Of course, if every franchise authority tried to

programs to cable program services."[56] That concern likewise animated Congress' statutory direction that rates for cable program services pricing practices be interdicted only if they are "unreasonable."

B. The Failure to Adopt A Bifurcated Structure Led to the Order's Overwhelming Complexity and Makes it Unworkable

The decision to proactively regulate all non-pay services led to a scheme that is profoundly complex. Although not explained in these terms, undoubtedly the Commission acted in responsible recognition of the need to try to "fix" some of the likeliest negative outcomes of a comprehensive regulatory scheme. First, and significantly, it required the back-up, cost-of-service election out of a need to address the large number of systems which inevitably could not fit neatly into the industry-wide averages reflected in the benchmark tables. Second, the unitary rate structure approach bled over to equipment, leaving the Commission with a program that requires nearly every franchising authority in the country to review extensive cost analysis for equipment "used to provide the basic tier."[57]

Third, it injected the Commission into the private market's choices for upgrades in plant and improvements in the quantity and quality of cable programming. With the price cap adjustment methodology still unreleased, and open questions as to how upgrades and channel additions will be allowed and accounted for,

[56] Besen at 44.

[57] As TCI's initial Comments demonstrated, this is a flatly wrong reading of the Act's treatment of equipment.

these complexities, which have profound implications for the future of the cable industry, have only begun to be addressed.

The Commission's utilization of a tier neutral regime necessarily makes the Order complex -- so complex that it will not work.[58] The Commission has set out to regulate the individual rates of nearly all of the more than 30,000 cable community units in operation across the country. By its own estimates, the rates of three-quarters of these firms will be affected. Setting aside the very real question whether the franchising authorities have the necessary resources to implement the tasks of benchmark compliance, cost regulation of equipment, and cost-of-service hearings which the Commission has assigned to them, the FCC's ability to fulfill its own obligations under the Order is in doubt. Even before one accounts for cost-of-service hearings that will eventuate, the complaint process for benchmark

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[58] Other aspects of the regulatory scheme contribute to this problem, including: 1) The Commission's volunteering itself as the default regulator for local authorities which choose not to take on the task; 2) granting individual subscribers the right to appeal decisions of local franchising authorities; 3) prohibiting local authorities and cable operators from informally negotiating and settling local disputes. The Act explicitly instructs the Commission to prescribe regulations that "[s]eek to reduce the administrative burdens on subscribers, cable operators, franchising authorities, and the Commission." Section 623(b)(2)(A). The legislative history stresses this point, directing the Commission to establish regulations for the basic tier that are "not cumbersome for the cable operator to implement nor for the relevant authorities to enforce." House Report at 83. Section 623(b)(2)(A) was specifically added to the Act in order to "encourage the Commission to simplify the regulatory process." H.R. Conf. Rep. No. 862, 102d Cong., 2d Sess. 62 (1992). Despite Congress' clear mandate, the Commission has adopted a regulatory regime that produces the opposite result.

and equipment compliance for the cable programming tier will very predictably inundate the Commission.[59] Both consumers and cable operators may have to wait years before determinations can be made. Further, Commission staff time will also be absorbed in hearing the appeals from local franchising authorities' rate decisions. Once the addition of costly and lengthy cost-of-service regulation is factored in, it is clear that pragmatic adjustments must be made if the regulatory scheme is to succeed.

By analogy, the Commission has never regulated or even tried to regulate the interstate rates of the 1,100 individual local telephone company subject to its jurisdiction. Realizing that it would be impossible to undertake a separate review of each telephone company rate, the Commission has always utilized some sort of pooling arrangement, either through Separations and Settlements or the NECA pool for access charges. The pragmatism reflected in the Commission's treatment of local telephone companies should counsel its reconsideration of the cable rate regulations.[60]

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[59] Even if additional appropriations are given to the FCC, it is far from clear that the necessary resources will be available. The Commission's budget estimates predicted that

The courts have held that "When Congress delegates a function to an agency . . . an important element of congressional purpose is that the function be carried out sensibly and efficiently."[61] Absent a reasonable assessment of the "social costs and benefits,"[62] agency regulations are deemed to be arbitrary and capricious. Because the Rate Order's overall scheme and procedures are so complex, costly, and burdensome to implement for all parties involved, the Commission must reconsider the Order. Modification of the Order to reflect the differing legislative schemes for basic and cable programming services would substantially further this process.

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[61] Cablevision Systems Development Co. v. Motion Picture Ass'n of America, Inc., 836 F.2d 599, 612, cert. denied, 487 U.S. 1235 (1988). This view is reflected in the Administrative Procedure Act (APA), which requires that reviewing courts find unlawful and set aside "agency action, findings, and conclusions found to be arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law." 5 U.S.C.§ 706(2)(A). According to the D.C. Circuit, this section of the APA requires that agency rules be set aside if data in the rulemaking record "[d]emonstrates that the rule constitutes such an unreasonable assessment of social costs and benefits as to be arbitrary and capricious." Thompson v. Clark, 741 F.2d 401, 405 (D.C. Cir. 1984).

[62] Thompson v. Clark, 741 F.2d 401, 405 (D.C. Cir. 1984).

VI. CONCLUSION

TCI respectfully submits that the Commission should reconsider the Order consistent with the comments contained herein.

Respectfully submitted,

TELE-COMMUNICATIONS, INC.

Sue D Blumenfeld

Philip L. Verveer
Sue D. Blumenfeld
Laurence D. Atlas
Melissa Newman

Willkie Farr & Gallagher
Three Lafayette Centre
Suite 600
1155 21st Street, NW
Washington, D.C. 20036-3384

Its Attorneys

June 21, 1993

APPENDIX

C&P TELEPHONE SERVICE AVAILABILITY UPDATE

SERVICE AVAILABILITY UPDATE

A Bell Atlantic Company
C&P Telephone

ISSUED BY: C&P Telephone

PREPARED FOR:

SERVICE AVAILABLE:
Answer Call

DESCRIPTION:
Automatic telephone answering service that helps prevent missed messages whenever you are away from home or on the phone.

DATE AVAILABLE:
Immediately -- customer authorization required.

13-02-003441527

AVAILABILITY NOTICE

The **Answer Call** telephone message service, a Bell Atlantic® IQ® Service from C&P Telephone, is now available within your area. Answer Call is an automatic answering service that takes messages through your existing touch-tone phones. This practical service also offers a range of advanced features designed to provide greater flexibility and convenience 24 hours a day. There is no additional maintenance or equipment needed for Answer Call, and you can access your mailbox from a 12-button, touch-tone equipped telephone. As a C&P Telephone customer, you may order this service immediately for as little as $6.50 a month.

SPECIAL INTRODUCTORY OFFER:

Order today to receive your Answer Call enhancements at no additional charge. For a limited time only.

Send no money now.
All charges will appear on your phone bill.

CONSUMER INFORMATION

Answer Call works with 12-button, touch-tone equipped phones with "*" and "#" keys, and has a total message capacity of 30 minutes.

There is a one-time $10.00 application fee for Answer Call. When you order, you'll pay no connection charge for Fixed Call Forwarding, which is recommended to operate Answer Call. Answer Call's monthly charge includes $2.00 for Fixed Call Forwarding.

Answer Call ring setting: You select the initial ring setting. You may hear one more ring than selected, and callers may hear up to two more rings. If you want to change your ring setting at a later date, there is a $10.80 charge to do so.

There will be no additional charge for Optional Busy Greeting even after the introductory period ends.

Special Delivery℠ Service and Reminder Service will be available for a small usage charge following the introductory period.

If you have measured or message rate phone service, a charge will apply each time a call is forwarded to Answer Call or you call to retrieve messages.

Call Waiting customers: Answer Call will automatically pick up a second incoming call when you use Tone Block to temporarily turn off Call Waiting. To activate Tone Block, simply dial *70. A third caller will either hear a busy signal or will be forwarded to Answer Call.

All rates and charges are for residential service, are before taxes, if applicable, and are subject to change.

A detailed instruction guide will be mailed to you upon receipt of your order. Answer Call is a Bell Atlantic® IQ® Service.

ORDER NEW AND IMPROVED ANSWER CALL TODAY!

A Bell Atlantic Company
C&P Telephone
Bell Atlantic Response Center
P.O. Box 676
Drexel Hill, PA 19026-9937